

In the Matter of

Application by Verizon New Jersey Inc.,  
Bell Atlantic Communications, Inc.  
(d/b/a Verizon Long Distance), NYNEX  
Long Distance Company (d/b/a Verizon  
Enterprise Solutions), Verizon Global  
Networks Inc., and Verizon Select Services  
Inc., for Authorization To Provide  
In-Region, InterLATA Services  
in New Jersey

## COMMENTS OF SPRINT COMMUNICATIONS COMPANY L.P.

January 14, 2002

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FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C. 20054

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Inc., for Authorization To Provide )  
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in New Jersey )

CC Docket No. 01-347

**COMMENTS OF SPRINT COMMUNICATIONS COMPANY L.P.**

Sprint Communications Company L.P. opposes the above-captioned application of Verizon for authorization to provide in-region, interLATA services in New Jersey.<sup>1</sup> The public interest requires that the application be denied unless the Commission is convinced that the local markets have been opened fully and irreversibly to competitive entry. In Sprint's view, this is not yet the case.

**I. INTRODUCTION AND SUMMARY.**

A key purpose of the 1996 amendments to the Communications Act of 1934 (the Act) was to open the local market to competition. To that end, Congress envisioned three avenues of local entry: resale, use of incumbent LEC unbundled network elements and

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<sup>1</sup> Application by Verizon New Jersey Inc., Bell Atlantic Communications, Inc. (d/b/a Verizon Long Distance), NYNEX Long Distance Company (d/b/a Verizon Enterprise Solutions), Verizon Global Networks Inc., and Verizon Select Services Inc., for Authorization to Provide In-Region, InterLATA Services in New Jersey, CC Docket No. 01-347 (filed December 20, 2001) (Application).

facilities-based competition; and it placed incumbent LECs in the rather unnatural role of assisting their would-be competitors by imposing the interconnection, resale, unbundling and collocation obligations of § 251(c).

To encourage the principal ILECs – the BOCs – to cooperate in this process, Congress enacted the “carrot” of § 271, giving the BOCs the right to enter the long distance market in-region once their local markets were truly open. The Commission recognized the importance of local market competition in one of the first applications it decided under this section.

Although Congress replaced the MFJ’s structural approach, Congress nonetheless acknowledged the principles underlying that approach that BOC entry into the long distance market would be anticompetitive unless the BOCs’ market power in the local market was first demonstrably eroded by eliminating barriers to local competition. \*\*\* In order to effectuate Congress’ intent, we must make certain that the BOCs have taken real, significant and irreversible steps to open their markets. We further note that Congress plainly realized that, in the absence of significant Commission rulemaking and enforcement, and incentives all directed at compelling incumbent LECs to share their economies of scale and scope with their rivals, it would be highly unlikely that competition would develop in local exchange and exchange access markets to any discernable degree.<sup>2</sup>

If the BOCs are allowed to enjoy the § 271 “carrot” before local competition is fully established, they will have little incentive to cooperate with competitive LECs thereafter, unless they are subject to continuing regulation. Successfully maintaining such a regulatory structure and adapting it to changes in technology will require significant on-going resources of both the Commission and interested parties, with, at best, uncertain

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<sup>2</sup> Application of Ameritech Michigan Pursuant to Section 271 of the Communications Act of 1934, as amended, To Provide In-Region, InterLATA Services In Michigan, 12 FCC Rcd 20543, ¶18 (1997) (Michigan Order).

results. It would be far preferable to withhold the § 271 “carrot” until local competition is sufficiently entrenched that competitive forces can supplant the intensive regulation and enforcement that otherwise would be required. Sprint does not believe that point has yet been reached in New Jersey.

In its application, Verizon states that it “disagrees as a legal matter that the Commission may conduct any analysis of local competition in its public-interest inquiry. Under the terms of the Act, the public-interest inquiry should focus on the market to be entered: the long distance market.”<sup>3</sup> The recent decision of the Court of Appeals for the District of Columbia concerning the FCC’s grant of SBC’s 271 application for long distance service in Kansas and Oklahoma remanding the “price squeeze” issue<sup>4</sup> disproves Verizon’s interpretation of the Act. The appellants argued that the low volume of residential customers in these states and SBC’s pricing which does not provide enough margin to make competition profitable are evidence of a “price squeeze” that is inconsistent with the public interest. In commenting on the Commission’s inadequate consideration of the appellants’ claim, the court stated: “Here, as the Act aims directly at stimulating competition, the public interest criterion may weigh more heavily towards addressing potential ‘price squeeze.’” *Id.* at [\*15]. Clearly, the court considers the Act’s goal of “stimulating competition” to refer to competition in the local market, which is the market affected adversely by a “price squeeze,” not the long distance market. Thus, it is

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<sup>3</sup> Application, page 77, footnote 70.

<sup>4</sup> Joint Application by SBC for Provision of In-Region, InterLATA Services in Kansas and Oklahoma, 16 FCC Rcd 6237 (2001), remanded, Sprint Communications Co. L.P. v. FCC, \_\_ F. 3d \_\_ (DC Cir. 2001), 2001 U.S. App. LEXIS 27292.

appropriate to consider whether the dismal state of competition and the low volume of residential customers served by facilities-based competitors is in the public interest when evaluating a 271 application.

As shown below, the CLEC industry is in a state of crisis, and the RBOCs have failed to establish themselves outside their territory. In New Jersey, residential competition, provided almost exclusively over resold Verizon facilities, has not been firmly established.

## **II. THE CLEC INDUSTRY IS IN A STATE OF CRISIS. (PUBLIC INTEREST)**

The past year has been marked by the bankruptcy of many of the CLECs that were in the vanguard of the industry: Covad, e-Spire, NorthPoint, Rhythms, Teligent, WinStar and Convergent, to name a few.<sup>5</sup> Most recently, on November 16, 2001, Net2000 filed voluntary petitions for relief under Chapter 11 and agreed to sell substantially all of its assets to Cavalier Telephone.<sup>6</sup> It comes as no surprise that a Morgan Stanley analyst recently released a "dismal report" about the state of the CLEC

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<sup>5</sup> For a more complete list of CLECs that have filed for bankruptcy, *see* Comments of Sprint Communications Company L.P., In the matter of Joint Application by BellSouth Corporation, Inc., BellSouth Telecommunications, Inc., and BellSouth Long Distance, Inc. for Provision of In-Region InterLATA Services in Georgia and Louisiana, CC Docket No. 01-277, filed October 19, 2001, p. 6.

<sup>6</sup> NET2000 Communications Inc (NTKK) Form 8-K, <http://biz.yahoo.com/e/011121/ntkk.html>.

industry, identifying several specific local carriers as likely candidates for formal restructuring.<sup>7</sup>

Faced with the expense and difficulty of building out local networks and with mounting losses, other CLECs have been forced to downsize. On October 3, 2001, McLeodUSA announced plans to reduce its workforce by 15 percent, consolidate 11 facilities into 3, sell non-core assets and excess inventory to generate between \$400 and \$450 million, and take a one-time non-cash charge of approximately \$2.9 billion.<sup>8</sup> In its December 3, 2001 announcement of its recapitalization and financial restructuring plan, McLeodUSA stated that “it may pursue the administrative convenience of the court system through a voluntary pre-packaged Chapter 11 in order to achieve retirement of all outstanding bond issues and to accomplish the recapitalization in an expeditious manner.”<sup>9</sup> Following McLeodUSA’s announcement, Reuters reported that McLeodUSA’s shares fell over 21 percent and “Moody’s Investor Service downgraded its distressed debt to one notch above its lowest grade.”<sup>10</sup>

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<sup>7</sup> Morgan Stanley: XO “Likely” to Restructure, Washtech.com, Brendan Barrett (October 9, 2001).

<sup>8</sup> McLeodUSA Press Room, “McLeodUSA Announces Focused Strategy for Future Growth, Abandons National Network, Identifies Non-Strategic Assets for Sale, Maintains Fully Funded Plan.”  
<http://www.mcleodusa.com/html/ir/singleStory.php3?pid=147&type=press>.

<sup>9</sup> McLeodUSA Press Room, “McLeodUSA Reaches Recapitalization Agreements with Forstmann Little and Secured Lenders.”  
<http://www.mcleodusa.com/html/ir/singleStory.php3?pid=151&type=press>.

<sup>10</sup> “McLeodUSA Shares Fall, Moody’s Downgrades Debt.”  
[http://dailynews.yahoo.com/h/nm/20011204/tc/telecoms\\_mcleodusa\\_dc\\_1.html](http://dailynews.yahoo.com/h/nm/20011204/tc/telecoms_mcleodusa_dc_1.html).

XO Communications, another major local competitor, recently laid off 600 employees, approximately 8 percent of its workforce.<sup>11</sup> On November 29, 2001, XO announced a proposed restructuring plan under which Forstmann Little & Co.'s initial investment of \$1.5 billion in preferred stock would be wiped out and it and Teléfonos de México S.A. de C.V. (TELMEX) would each invest \$400 million in exchange for a 39 percent share in the company. The restructuring comes with a high price to other shareholders and bond holders. According to a recent article in The Wall Street Journal, the investment "is part of a proposed restructuring plan, which in its current state would wipe out founder Craig McCaw's investment, leave other shareholders virtually penniless and require bondholders to take a big hit."<sup>12</sup>

Other CLECs that Verizon has identified as among those competing in New Jersey are also in financial difficulty. For example, on December 26, 2001, eLEC announced that it had received a Nasdaq Staff Determination that it "fails to comply with the minimum net tangible assets or minimum stockholders' equity requirements for continued listing" and is subject to delisting from The Nasdaq SmallCap Market.<sup>13</sup> On

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<sup>11</sup> XO Communications Lays Off 600; CLEC-Planet, Wayne Kawamoto (October 3, 2001).

<sup>12</sup> Kara Scannell, "Forstmann Bets Even More of Its Money on XO," The Wall Street Journal, November 30, 2001, p. C1. Similarly, Simon Romero of The New York Times wrote that Forstmann's proposals for McLeodUSA and XO, "which largely plunder shareholders and bondholders, have sent a chill through a part of the telecommunications industry already in tatters." "A Buyout Company May Plan Some Tough Love for Two Telecoms, and Holders of Their Debt and Stock," December 10, 2001, p. C3.

<sup>13</sup> "eLEC Receives Notification From the Nasdaq Listing Qualifications Department," [http://www.elec.net/index.cfm?sTitle=&sElec=53&grab\\_document=136](http://www.elec.net/index.cfm?sTitle=&sElec=53&grab_document=136).



January 2, 2002, Network Plus issued a press release stating that it is in discussions with its lenders about restructuring its senior credit facility and has “engaged UBS Warburg LLC to examine financial and restructuring alternatives for Network Plus.”<sup>14</sup> It warned that if it is unsuccessful in finding the debt and equity financing it requires, “Network Plus may default under its senior credit facility or may be required to substantially modify its current business plan, including reducing or terminating all or significant portions of its operations and any planned expansion.” Id. And on January 3, 2002, Adelphia Business Solutions announced that “it will not make the payment-in-kind dividend scheduled for January 15, 2002 on its 12 7/8% Senior Exchangeable Redeemable Preferred Stock (the “Preferred Stock”). Under the terms of the preferred stock, dividends will continue to accrue until paid.”<sup>15</sup>

With CLECs under these severe financial difficulties, investors have unambiguously indicated that they will remain wary of CLEC stocks until it becomes clearer “which CLECs will survive the carnage.”<sup>16</sup> Industry experts agree that when the

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<sup>14</sup> “Network Plus Enters Into Limited Waiver with Its Senior Lenders and Announces Engagement of USB Warburg,” [http://www.corporate-ir.net/ireye/ir\\_site.zhtml?ticker=NPLS&script=410&layout=-6&item\\_id=241716](http://www.corporate-ir.net/ireye/ir_site.zhtml?ticker=NPLS&script=410&layout=-6&item_id=241716). *See also*, “Limited Waiver Is Received On Terms of Credit Facility,” The Wall Street Journal, January 3, 2002, p. C12.

<sup>15</sup> “Adelphia Business Solutions, Inc. Suspends Payment-in-Kind Dividend on Preferred Stock,” [http://www.adelphia.com/invest/pdf/abiz\\_preferred.pdf](http://www.adelphia.com/invest/pdf/abiz_preferred.pdf). *See also*, “Comm Daily® Notebook,” Communications Daily, January 7, 2002, pp. 6-7.

<sup>16</sup> Telecom Services – Local: Hoexter’s Broadband Bits, Merrill Lynch Capital markets, K. Hoexter, at \*1 (June 18, 2001).

smoke clears from “the steady stream of Chapter 11 filings in the competitive telecom sector” only a few CLEC companies will remain.<sup>17</sup>

### **III. OUT OF REGION RBOCs HAVE FAILED TO COMPETE AGAINST FELLOW RBOCs. (PUBLIC INTEREST)**

Perhaps the best indicator of the state of local competition is the extent to which ILECs choose to compete with each other. ILECs not only know the local market, but they come equipped with the complex back-office systems needed to provide service efficiently and economically. It is telling, then, that despite earlier assertions to the contrary, the RBOCs have remained largely outside the local competition fray. Verizon does not identify any fellow RBOC as a competitor to it in New Jersey. Qwest, SBC and BellSouth have failed to establish themselves as significant providers of local service outside their serving territories. If local competition were truly enabled, these RBOCs could have entered New Jersey and other Verizon markets with bundles of local and long distance service. Perhaps Sprint’s experiences can shed some insight into why they have not done so.

Despite its extensive experience in the local markets as an incumbent LEC, Sprint has no significant CLEC operations today. On the contrary, Sprint has cut back significantly on its previously planned CLEC activities. One year ago, Sprint abandoned its local market entry via resale or UNE-P altogether. After efforts in selected states (including Georgia, New York, Texas and California), Sprint determined that entry through either of these means could not be profitable, even taking into account its ability

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<sup>17</sup> Telecom Services – Alternative Carriers: Competition Telecom, Morgan Stanley, Dean Witter, P. Kennedy, at \*1 (June 19, 2001).

to retain long distance customer accounts. In October of this year, Sprint announced the discontinuance of its Sprint ION residential and business offerings. Sprint had viewed Sprint ION as a breakthrough, integrated offering that promised to give consumers a superior alternative to the local offerings of ILECs. However, after extensive testing, including commercial offering of the service in a number of states, Sprint determined that it could not economically justify continuation or expansion of the service.

Among the factors contributing to Sprint's decision was the difficulty of obtaining the "last mile" facilities needed for the service from the RBOCs. No Bell Company has found it to be in its own interest to cooperate in establishing local competition. Thus, at every turn, there are lengthy delays, inadequate provision of service, and high prices. Due to the regulatory and legislative uncertainties regarding the future availability of facilities, carriers have no assurance about the level of future rates or the availability of services and service elements. Making business decisions to expend massive amounts of capital is, in the face of such uncertainties, obviously very risky.

#### **IV. RESIDENTIAL COMPETITION IN NEW JERSEY HAS NOT BEEN FIRMLY ESTABLISHED. (PUBLIC INTEREST)**

As noted above, the Act allows competitors to enter the local market via three entry strategies: resale of the incumbent's network, the use of unbundled network elements, or interconnection to the incumbent's network by pure facilities-based providers, or some combination thereof. The Commission has found that all three means of entry should be available:

Congress did not explicitly or implicitly express a preference for one particular strategy, but rather sought to ensure that all procompetitive entry strategies are available. Our public interest analysis of a section 271 application, consequently,

must include an assessment of whether all procompetitive entry strategies are available to new entrants.

Michigan 271 Order ¶387. In discussing how it would evaluate whether all strategies are available, the Commission made clear that there should be competition in each means of providing competitive local service and to both business and residential customers:

The most probative evidence that all entry strategies are available would be that new entrants are actually offering competitive local telecommunications services to different classes of customers (residential and business) through a variety of arrangements (that is, through resale, unbundled elements, interconnection with the incumbent's network, or some combination thereof), in different geographic regions (urban, suburban, and rural) in the relevant state, and at different scales of operation (small and large).

Id. ¶391.

Although Verizon claims that meaningful residential competition exists, there are several flaws in its arguments. In its application, Verizon states that there are "at least 20 competing carriers in New Jersey that actively provide service either wholly or partially over facilities they have deployed themselves." Application at 6. Verizon estimates that competitors serve approximately 564,000 lines, of which 507,000 are business lines. Id. at 79. The remaining 57,000 lines are residential.<sup>18</sup> Dr. Taylor states that 55,000 of these lines, or 96 percent, are provided over resold facilities. Id. ¶ 22.

Verizon's data demonstrate that residential service in New Jersey is sorely lacking. The 57,000 residential lines represent 0.9% of the loops of the Bell Company in New Jersey as of December 31, 1999.<sup>19</sup> Further, 96 percent of the lines are provided over

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<sup>18</sup> Declaration of William E. Taylor, "Local Competition in New Jersey," Application, Appendix A, Tab F, ¶ 4.

<sup>19</sup> Trends in Telephone Service, Industry Analysis Division, Common Carrier Bureau, August 2001, Table 8.2.

resold facilities, indicating that these carriers are not willing to make a sizeable investment to serve this market. The State of New Jersey Ratepayer Advocate also found that Verizon has not met the standards for approval to enter the long-distance market and that “more time is needed to determine if competition will develop in the local exchange market ...”<sup>20</sup> According to Ratepayer Advocate Blossom A. Peretz, “Our concern is that if the FCC grants Verizon long-distance authority based on the Board’s recommendation, competition may not get a chance to emerge in New Jersey, and consumers will not get the opportunity to enjoy the benefits of choice.” Id.

Thus, competition for residential customers is nascent, and competition in forms other than resale is negligible. This negligible amount of facilities-based competition in the residential market falls far short of demonstrating that local residential competition has been fully and irreversibly enabled; and, until it is, the public interest is not satisfied by giving Verizon the “carrot,” § 271 authority.

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<sup>20</sup> State of New Jersey Division of the Ratepayer Advocate, “Ratepayer Advocate Disappointed the BPU Votes to Recommend to the FCC Verizon’s Application to Offer Long-Distance Service in New Jersey,” released January 9, 2002.  
<http://www.rpa.state.nj.us/010902.htm>.

**V. CONCLUSION.**

Because Verizon has failed to demonstrate that there is meaningful competition in New Jersey, its application for Section 271 relief should be denied.

Respectfully submitted,

Sprint Communications Company L.P.



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January 14, 2002

### CERTIFICATE OF SERVICE

I, Sharon Kirby, do hereby certify that this 14th day of January 2002 copies of the Comments of Sprint Communications Company L.P. on the application by Verizon for Section 271 Authorization to Provide In-Region, InterLATA Service in the State of New Jersey, CC Docket No. 01-347, will be delivered as indicated below to the following parties:

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